Supreme Court, U.S.
FILED

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NO. _____

**IN THE SUPREME COURT OF THE UNITED STATES**
**October Term, 1996**

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SMILECARE DENTAL GROUP,

PETITIONER,

vs.

DELTA DENTAL PLAN OF CALIFORNIA, INC.,

RESPONDENT.

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On Petition for Writ of Certiorari
to the United States Court of Appeals
for the Ninth Circuit

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# PETITION FOR WRIT OF CERTIORARI

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71 pp

## QUESTION PRESENTED

Whether a complex antitrust case should be resolved by a motion to dismiss when doing so requires deciding intensive factual issues (including a determination of the competitors in the relevant market, the anticompetitive effect of defendant's alleged misconduct, and whether the defendant acted with legitimate business justification) solely upon the complaint's allegations and the court's surmises about how the markets in question operate?

## LIST OF PARTIES

All parties appear in the caption of the case on the cover page.

Pursuant to Supreme Court Rule 29(6), the petitioner states that neither party to this proceeding has any nonwholly owned subsidiaries or any parent companies.

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## IN THE SUPREME COURT OF THE UNITED STATES
**October Term, 1996**

## PETITION FOR WRIT OF CERTIORARI

Petitioner SmileCare Dental Group respectfully petitions that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Ninth Circuit.

## OPINIONS BELOW

The opinion of the Court of Appeals is reported at 88 F.3d 780 (9th Cir. 1996), and is reproduced at Appendix A to the petition. The opinion of the United States District Court is reported at 858 F. Supp. 1035 (C.D. Cal. 1994), and is reproduced at Appendix B to the petition.

## JURISDICTION

The United States Court of Appeals for the Ninth Circuit entered its judgment and filed its opinion on July 5, 1996. No petition for rehearing was filed. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

## STATUTORY AND OTHER PROVISIONS INVOLVED

Section 2 of the Sherman Act, 15 U.S.C. § 2, provides in relevant part: "Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several

States . . . shall be deemed guilty of a felony . . . ."

Federal Rule of Civil Procedure 12(b)(6) provides in relevant part: "[T]he following defenses may at the option of the pleader be made by motion: . . . (6) failure to state a claim upon which relief can be granted. . . . "

## STATEMENT OF THE CASE

A. Introduction

In California, dental health plans contract with dentists to provide services to patients who purchase -- either out of their own pocket or by way of their employer or union -- coverage under the plan. Petitioner SmileCare Dental Group ("SmileCare") is a dental plan that sued another dental plan, respondent Delta Dental Plan of California, Inc. ("Delta"), for alleged monopolistic practices.[1] Delta brought a motion to dismiss under Federal Rule of Civil Procedure 12(b)(6), which the district court granted. The Court of Appeals for the Ninth Circuit affirmed on the grounds that, as a matter of law, 1) SmileCare and Delta do not compete with each other as providers of dental plan coverage; 2) Delta's conduct was not anticompetitive; and 3) Delta acted with legitimate business justification.

B. Factual Background

Delta is the dominant dental plan in California, covering 60% of all Californians who have dental coverage and one of every three persons in California regardless whether he or she has coverage. First

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[1] The particularities of California law distinguish dental or health care plans, such as the parties to this case, from insurers on the basis of specific criteria not relevant to this case. See generally California Health & Safety Code § 1340 et seq. In economic terms, one could analyze this case as if SmileCare and Delta were the sort of dental insurers prevalent in other parts of the country.

Amended Complaint (reproduced as Appendix C) at ¶¶ 4-5. This dominant position allows Delta to sign up almost every dentist in California (95%) as a nonexclusive "provider" of dental services. Id. at ¶ 6. Given Delta's predominance, dentists have become dependent upon being a Delta provider, and not being a Delta provider would inflict serious competitive disadvantage on any particular dentist. Id. Delta thus has monopoly power among California dental plans, a fact which Delta does not dispute for present purposes.

While Delta offers a traditional full indemnity plan obligating it to pay 100% of the patient's cost for dental services, the vast majority of Delta's policies are co-payment plans. Id. at ¶ 8. Under these plans, Delta's contracts with dentists state that Delta will pay only a percentage of the dentist's total charge and require the dentist to collect directly from the patient the remainder of the charge. Id. The contracts prohibit dentists from waiving the co-payment. Id.

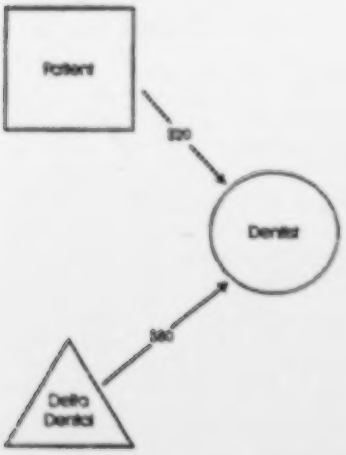
SmileCare also offers a traditional, full indemnity primary dental plan, but provides most of its coverage in the form of "supplemental dental plans." Id. at ¶ 9. Many who purchase SmileCare's supplemental dental plans also use Delta's co-payment plan for their primary dental coverage. Id. Under the supplemental plan, the consumer pays a monthly fee to SmileCare and agrees to use a SmileCare dentist. Id. at ¶ 10. The patient then makes no separate co-payment to the dentist; instead, the dentist receives a monthly capitation payment from SmileCare based on the total number of patients served. In essence, rather than accepting a larger co-payment from those patients who happen to use the dentist's services that month, the dentist under the supplemental plan accepts a smaller capitation payment on behalf of all the SmileCare patients the dentist serves, regardless whether the patients come into the dentist's office that month.

At oral argument before the Ninth Circuit, Delta's attorneys presented a chart virtually identical to that set forth below. The chart shows how a hypothetical patient under a Delta co-payment plan who needs $100 of services was treated, absent Delta's anticompetitive conduct, depending on whether the patient also is covered by SmileCare's supplemental dental plan:

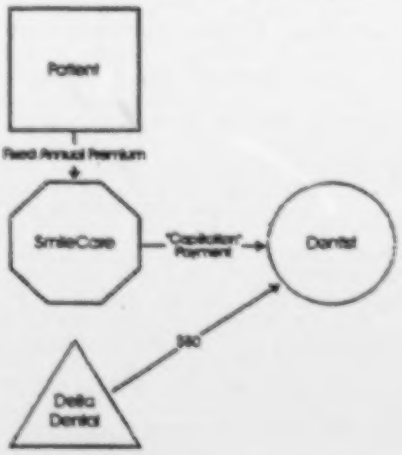
$100 IN DENTAL SERVICES WITH $20 CO-PAYMENT

Patient Has:

Delta Coverage Only




Delta and SmileCare Coverage




The California Department of Corporations approved the actuarial soundness of SmileCare's supplemental dental plan over Delta's objections. Id. at ¶ 13.

The allegations in SmileCare's complaint, which must be taken as true for present purposes, are as follows. Delta treated a dentist's acceptance of the monthly capitation payment from SmileCare, rather than the patient's out-of-pocket lump sum payment, as an impermissible "waiver" of the co-payment in breach of the provider agreement between Delta and the dentist. Id. at ¶ 11. When

dentists accepted the capitation payment, Delta responded by slashing to noncompensatory levels the reimbursements to SmileCare dentists, threatening to terminate dentists and actually terminating at least some SmileCare dentists. Id. at ¶¶ 11-12. Delta undertook this conduct with the purpose and effect of maintaining its monopoly over dental plans in California. Id. Delta induced dentists to refuse to perform services for patients under SmileCare's supplemental dental plan in order to eliminate that plan as an option in the marketplace. Id. at ¶¶ 14-15. As a result, consumers were deprived of coverage for the full cost of dental care, suffered a reduction of dental services and paid more for dental care. Id. at ¶ 22. In short, Delta used its monopoly power in an attempt to squeeze SmileCare out of the market by coercing dentists into not accepting SmileCare patients.

C. Proceedings Below

SmileCare filed its complaint on September 8, 1993. Delta moved to dismiss under Fed. R. Civ. P. 12(b)(6), arguing that the complaint failed to state a claim in that Delta's conduct could not have the requisite anticompetitive effect. After the district court granted the initial motion to dismiss, SmileCare filed the first amended complaint at issue here. After Delta renewed its motion, the district court dismissed the amended complaint with prejudice on July 25, 1994, in a published opinion. Appendix B.

SmileCare filed a timely notice of appeal. On July 5, 1996, the Ninth Circuit Court of Appeals affirmed, per Circuit Judge T.G. Nelson and Eugene F. Lynch, a United States District Judge sitting by designation. Circuit Judge Harry Pregerson dissented. The majority opinion started from the premise that the question "[w]hether specific conduct is anticompetitive is a question of law." Appendix A at A-8. The court then identified the "key issue" as "whether Delta Dental's refusal to recognize as contractually valid a participating dentist's

acceptance of co-payment from a supplemental insurer rather than from the patient herself has any impermissible anticompetitive effects." Id. at A-10. The appellate court -- based not upon evidence but upon the complaint's allegations and the court's own conjecture about how the market for dental plans operates -- made three important rulings:

1. Delta's conduct had no anticompetitive effect, as a matter of law. Id. at A-12 to A-13. Rather, the Ninth Circuit concluded that Delta actually promoted competition in refusing to accept the SmileCare capitation payment as a co-payment.[2] Id. at A-13

2. Delta and SmileCare were not competitors, as a matter of law, because SmileCare's supplemental dental plan provides reimbursement only for the co-payment, not for the primary coverage provided by Delta. Id. at A-14.

3. Delta's conduct was justified by legitimate business purposes, as a matter of law. Id. at A-17.

Judge Pregerson dissented:

> [W]hat the district court has really done is to ignore the rule that on a motion to dismiss facts alleged by the nonmoving party are presumed true. Instead of taking as true all of SmileCare's allegations about

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[2] The Ninth Circuit relied heavily on two cases holding that the Employee Retirement Income Security Act (ERISA) did not prohibit insurers from requiring that providers neither waive co-payments nor assign them out of existence. Davidowitz v. Delta Dental Plan, Inc., 946 F.2d 1476, 1479 (9th Cir. 1991); Kennedy v. Connecticut General Life Insurance Co., 924 F.2d 698 (7th Cir. 1991). That authority is irrelevant to the present case because, as the dissent noted: "The purpose of ERISA is to protect employee benefits. By contrast, the purpose of the Sherman Act is to protect competition." Appendix A at A-18 (Pregerson, J., dissenting). Two statutes with such clearly different purposes necessarily require completely different lines of inquiry.

> the anticompetitive effects of Delta's conduct, the district court has turned the standard on its head by taking only Delta's asserted defense as true. It is improper for the court to make such an evaluation of asserted defenses at this stage in the proceedings.

Id. at A-20 (citation omitted).

## REASON FOR GRANTING THE PETITION

### A. The Ninth Circuit's Determination of Factual Questions on the Basis of Allegations in the Complaint and Economic Surmise Conflicts with Relevant Decisions of This Court

Supreme Court Rule 10(c) states that a factor weighing in favor of granting a petition for writ of certiorari is that a Court of Appeals "has decided an important federal question in a way that conflicts with relevant decisions of this Court." In this case, the Ninth Circuit rendered a decision that conflicts with important decisions of this Court directing lower courts to resolve monopolization cases on the basis of evidence, not by applying potentially dubious economic reasoning to a sketchy or nonexistent factual record.

Analysis of the conflict between the Ninth Circuit's decision and this Court's monopolization case law starts with Matsushita Electric Industrial Co. v. Zenith Radio Corp., 475 U.S. 574 (1986). In Matsushita, American electronics manufacturers alleged that Japanese competitors conspired for 20 years to price below cost in the United States in expectation of expanding their market share in the future. After detailed discovery had taken place, the Court found untenable plaintiffs' theory that the Japanese manufacturers had taken 20 years of losses on the glimmer of hope that they might someday

recoup those losses. Id. at 587-88, 595-98. Accordingly, the Court held that a reasonable jury could not return a verdict for plaintiffs and that summary judgment would be appropriate. Id.

Unfortunately, too many lower courts used Matsushita as an excuse to run wild, exceeding the bounds of a common sense precedent by granting summary judgment or dismissing claims that should have been tried. See Stephen Calkins, Supreme Court Antitrust 1991-92: The Revenge of the Amici, 61 Antitrust L.J. 269, 298 (1993) ("Many courts have viewed [Matsushita] as a license for the trial court to examine plaintiffs' theories critically at early stages of litigation. Matsushita emboldened courts to address the merits at early stages. . . ." (footnote omitted)).

This Court clarified Matsushita in Eastman Kodak Co. v. Image Technical Services, Inc., 504 U.S. 451 (1992). In Kodak, plaintiff independent service organizations alleged that a manufacturer had cut off their parts supplies so that the manufacturer could remain virtually the sole service provider for the equipment. The district court had granted summary judgment on the basis of the manufacturer's economic argument purportedly demonstrating that competition among manufacturers ensured that service customers would suffer no anticompetitive effects. The Supreme Court rejected the idea that the argument was true in every case as a matter of law and held that summary judgment had been improperly granted.

> Legal presumptions that rest on formalistic distinctions rather than actual market realities are generally disfavored in antitrust law. This Court has preferred to resolve antitrust claims on a case-by-case basis, focusing on the 'particular facts disclosed by the record.' Maple Flooring Manufacturers Assn. v. United States, 268 U.S. 563, 579 (1925). . . .

Id. at 466-67.

The Court went on to explicitly state that Matsushita had not created a new rule of summary judgment in antitrust cases, but was merely an application of the general summary judgment standard that a "nonmoving party's inferences [must] be reasonable in order to reach the jury." Id. at 468.

The result reached by the Ninth Circuit here conflicts with Kodak's insistence -- based on precedent as time-honored as Maple Flooring -- that antitrust claims be resolved upon evidence rather than upon conjecture loosely based on economic analysis. Indeed, the Ninth Circuit's use of economic conjecture in this case is worse than that which was rejected in Kodak. At least in Kodak plaintiffs had undertaken some discovery. Here the motion to dismiss was granted and upheld before any discovery could be taken.

Each of the three bases on which the Ninth Circuit relied to dismiss this case reflected an impermissible preference for theoretical speculation over evidentiary proof. First, in ruling that Delta's conduct had no anticompetitive effects, the Ninth Circuit conjectured that Delta's refusal to allow dentists to capitate the co-payment benefitted rather than harmed competition. Although a jury considering all the (yet undiscovered) evidence about the operation of the relevant market might accept Delta's argument, that argument is certainly not true as a matter of law.[3] Consider the plight of the consumer who prefers handling the co-payment responsibility by

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[3] The Ninth Circuit seemed particularly confused on this point. It reasoned that Delta's refusal to allow dentists to accept capitation payments as co-payments was legal because Delta was simply enforcing a contractual right. Appendix A at A-11 to A-12. Such reasoning is circular, however, because whether the contractual provision is legal as enforced was precisely the question to be determined in this case.

paying small monthly premiums to SmileCare rather than large lump sums to the dentist when services are needed. After Delta successfully squeezes SmileCare out of the market, that consumer will take little comfort from the Ninth Circuit's breezy assurance that the effect of Delta's conduct is not anticompetitive.

In fact, a monopolist's restriction on "consumer preferences in setting output and prices is more important than higher prices and lower output, per se, in determining whether there has been an injury to competition." Sullivan v. National Football League, 34 F.3d 1091, 1101 (1st Cir. 1994) (citing NCAA v. Board of Regents of University of Oklahoma, 468 U.S. 85, 107 (1984)), cert. denied, ___ U.S. ___, 115 S. Ct. 1252 (1995). In restricting consumer choice by eliminating the capitation option, Delta undertook what falls squarely within the definition of anticompetitive conduct.

Second, in ruling that Delta and SmileCare are not competitors, the Ninth Circuit usurped the role of the jury. A jury hearing all the evidence about competition in California's market for dental plans would be free to conclude that Delta and SmileCare are not competitors. But it cannot be said as a matter of law that two dental plans, both of which cover patients in California, are not competitors. Delta admitted that it might respond to SmileCare's supplemental plan -- assuming it could not squeeze SmileCare out of the market by its current anticompetitive campaign -- by altering the terms of Delta's primary dental coverage. See Appellant's Brief to the Ninth Circuit at 20 n.13, 34 n.21. Obviously such alterations would change the dynamic of the competitive struggle between Delta's primary dental plan and SmileCare's. The jury could reasonably rely on this fact alone to conclude that Delta and SmileCare compete. See United States v. Syufy Enterprises, 903 F.2d 659, 663 (9th Cir. 1990) (competitors are those that impose "an essential discipline on

producers and sellers of goods to provide the consumer with a better product at a lower cost"); Thurman Industries, Inc. v. Pay 'N Pak Stores, Inc., 875 F.2d 1369, 1374 (9th Cir. 1989) ("field of competition [includes] the group or groups of sellers or producers who have actual or potential ability to deprive each other of significant levels of business"). Unless this petition is granted, however, the jury will never have that opportunity.

Third, the Ninth Circuit's determination that Delta's conduct was excused by legitimate business justifications conflicts not only with this Court's decision in Kodak but also with Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985). In Aspen, the Court determined that whether a monopolist's conduct was justified by a legitimate business purpose was a question of fact for the jury. Id. at 608-11. The Court stated that, in making that determination, the jury could rely upon the monopolist's subjective intent as revealed by its admissions or surrounding circumstances. Id. at 608 n.39. Although the Ninth Circuit admitted that the question of legitimate business justification is ordinarily one of fact, it called the issue a "foregone conclusion," citing to an earlier Ninth Circuit opinion upholding a contractual provision forbidding waiver of co-payments from an attack under ERISA. Appendix A at A-17. Obviously, an earlier Ninth Circuit opinion says nothing about Delta's subjective intent and thus cannot resolve this factual question.

One hypothetical example reveals the fundamental problem with the Ninth Circuit's opinion. Suppose for the moment that Delta's files contain a detailed study by competent executives analyzing the effect of SmileCare's supplemental dental plan on Delta's business. This hypothetical study reasonably concludes that SmileCare's supplemental plan increases the sales of Delta co-payment plans because the supplement makes Delta's plans attractive to consumers

who otherwise would be deterred by their distaste for lump sum co-payments. The hypothetical study also concludes that Delta should nonetheless forego the increased sales and undertake the conduct alleged in the complaint because of the benefits to Delta of eliminating SmileCare from the market.

Such a study by itself would refute all three of the bases for the Ninth Circuit's opinion. Yet the Ninth Circuit's decision to resolve these factual issues upon a motion to dismiss, before any discovery can be taken, means that such a study, if it exists, will never see the light of day.

The Ninth Circuit's approach does more than merely reach an unjust result in this particular case. It is a direct assault on this Court's antitrust jurisprudence as enshrined in Kodak and Aspen. In those cases, this Court made clear that antitrust cases should be resolved by fact-finders upon evidence, not by judges conjecturing with economic mumbo jumbo. As shown above, Kodak went so far as to remind lower courts that Matsushita set forth no contrary rule. The present case demonstrates that some lower courts still did not get the message. Unless this Court makes a strong statement about the proper circumstances for dismissing antitrust cases before trial, some lower courts will continue to usurp the role of the jury. They will

distort antitrust doctrine, to the ultimate detriment of the consumers whom the Sherman Act was designed to protect.

## CONCLUSION

The petition for a writ of certiorari should be granted.

Date: October 3, 1996

Respectfully submitted,

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# APPENDICES

FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

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SmileCare Dental Group,
*Plaintiff-Appellant,*

v.

Delta Dental Plan of California, Inc.,
*Defendant-Appellee.*

No. 94-56191

D.C. No.
CV-93-05437- RG

OPINION

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Appeal from the United States District Court
for the Central District of California
Richard A. Gadbois, Jr., District Judge, Presiding

Argued and Submitted
March 4, 1996 -- Pasadena, California

Filed July 5, 1996

Before: Harry Pregerson and Thomas G. Nelson,
Circuit Judges, and Eugene F. Lynch,* District Judge.

Opinion by Judge T.G. Nelson;
Dissent by Judge Pregerson

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**SUMMARY**

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*Honorable Eugene F. Lynch, United States District Judge for the Northern District of California, sitting by designation.

**Antitrust/Sherman Act/Health**

The court of appeals affirmed a district court dismissal for failure to state a claim. The court held that a dental insurer's refusal to recognize as contractually valid a dentist's receipt of co-payments from a supplemental insurer is not impermissible anticompetitive activity.

Appellee Delta Dental Plan of California, Inc., a dental insurer, offered a co-payment plan under which it paid participating dentists a portion of their fee and required them to collect the remainder, or co-payment, from their patients at the time of service. Appellant SmileCare Dental Group offered a supplemental plan which provided coverage for the co-payment.

Delta Dental did not recognize the co-payments made by supplemental insurers as contractually valid and deemed participating dentists who accepted such payments to be in breach of contract.

SmileCare sued Delta Dental in federal court, alleging that Delta Dental's policy violated the Sherman Act because it illegitimately restricted competition and was aimed at eliminating SmileCare's supplemental dental plan. Delta Dental moved to dismiss for failure to state a claim. The district court dismissed SmileCare's claims with prejudice, and SmileCare appealed.

[1] Whether specific conduct is anticompetitive is a question of law . Dismissal for failure to state a claim is appropriate where the complaint states not set of facts which, if true , would constitute an antitrust offense, notwithstanding conclusory language regarding the

elimination of competition and improper purpose.

[2] The key issue was whether Delta Dental's refusal to recognize as contractually valid a participating dentist's acceptance of co-payment from SmileCare rather than from the patient had any impermissible anticompetitive effects.

[3] The district court denied as matter of law SmileCare's argument that Delta Dental's conduct was anticompetitive based on its finding that SmileCare's supplemental insurance plan does not compete with Delta Dental's primary plan. [4] Instead of competing with Delta Dental directly, SmileCare would "discipline" Delta Dental by encroaching upon its method of disciplining its insureds. SmileCare and Delta Dental are not true competitors. Rather, SmileCare found a niche in the coverage "gap" created by the co-payment plan and sought to impose on Delta Dental its own way of doing business. SmileCare failed to cite any provision of the antitrust laws that would require Delta Dental to modify a legitimate way of doing business to allow SmileCare to sell its plan.

[5] Even assuming they were competitors, SmileCare's claims that Delta Dental's conduct amounted to "group boycott" or "refusal to deal" were not persuasive. [6] SmileCare's failure to allege the essential element of conspiracy between Delta Dental and any other parties precluded a group boycott claim. [7] It was well-established that competitors do not have a general duty to deal with one another.

[8] While the existence of valid business reasons is ordinarily a questions of fact, in this case it was a foregone conclusion requiring no further analysis: the validity of Delta Dental's business reasons for

requiring its dentists to collect the co-payment directly from the patient had already been established. Delta Dental's policy was supported as a matter of law by a legitimate business justification, its interest in protecting the disciplinary effect of its co-payment plan.

[9] Because Delta Dental's co-payment plan was concededly legitimate and because SmileCare failed to allege that Delta Dental's enforcement of its no-waiver clause had any anticompetitive effects, the complaint was properly dismissed. Circuit Judge Pregerson dissented, expressing the belief that SmileCare alleged facts which, if proved, could entitle it to relief under the antitrust laws because it was improper, on a motion to dismiss, to conclude that Delta Dental and SmileCare were not competitors and to find that a business justification existed for Delta Dental's refusal to accept SmileCare's supplemental payments.

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## COUNSEL

Maxwell M. Blecher, Blecher & Collins, Los Angeles, California, for the plaintiff-appellant.

Matthew L. Larrabee, Heller, Ehrman, White & McAuliffe, San Francisco, California, for the defendant-appellee.

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## OPINION

T.G. Nelson, Circuit Judge:

SmileCare Dental Group ("SmileCare") and Delta Dental Plan of California, Inc. ("Delta Dental") are dental insurers offering health care plans to employers, labor unions, and individuals. Delta Dental offers a co-payment plan under which it pays participating dentists a portion of their fee and requires them in return to collect the remainder, or co-payment, from their patients at the time of service. SmileCare offers a supplemental plan which provides coverage for the co-payment. Delta Dental does not recognize co-payments made by supplemental insurers as contractually valid, and deems participating dentists who accept such payments to be in breach of contract.

SmileCare appeals the district court's dismissal for failure to state a claim, alleging that Delta Dental's policy violates Section 2 of the Sherman Act, 15 U.S.C. § 2, because it illegitimately restricts competition and is aimed at eliminating SmileCare's supplemental dental plan. *Amici* Travelers Insurance Co., Prudential Insurance Co. of America and Golden Rule Insurance Co. appear in support of Delta Dental. We have jurisdiction pursuant to 28 U.S.C. § 1291, and we affirm.

## FACTS AND PROCEDURAL HISTORY

Both parties are dental insurers offering a variety of health care plans to employers, labor unions and individuals. According to SmileCare, sixty percent of all California residents with dental insurance are covered by Delta Dental. Ninety-five percent of California dentists are enrolled, on a nonexclusive basis, as Delta Dental service providers. Delta Dental offers a full coverage plan, but covers most of its insureds through its co-payment plans, which are considerably cheaper. Under the co-payment plan, Delta Dental pays participating dentists a portion of their fee and requires that the dentists recover the remainder directly from the patient as a co-payment. Dentists set their own fees, subject to approval by Delta Dental, and Delta Dental determines the amount of co-payment required according to the type of treatment performed. Delta Dental's contract with its service providers prohibits them from waiving the co-payment.

SmileCare offers a variety of dental health plans, but its primary business is a coverage plan called "SmileCare Coverage Plus," which is designed to supplement co-payments plans such as Delta Dental's. By paying participating dentists the co-payment, or an agreed-upon portion of the co-payment. Coverage Plus purports to fulfill the patient's payment obligations to the dentist. Coverage Plus subscribers are thereby provided with full dental coverage. According to SmileCare, Delta Dental has acted to thwart SmileCare and injure the consumer by refusing to accept co-payments from supplemental insurers. Delta Dental providers who accept SmileCare payments in lieu of patient co-payments are deemed by Delta Dental to be in breach of contract, and are allegedly penalized with reduced fee

payments, threats of termination, and, in some cases, actual termination.[1]

SmileCare filed its first complaint against Delta Dental on September 8, 1993, alleging a violation of Section 2 of the Sherman Act. The complaint also alleged various causes of action under state law, which, as noted above, are not at issue on appeal. The district court granted Delta Dental's motion to dismiss with leave to amend. SmileCare's amended complaint, filed on February 25, 1994, alleged virtually the same factual predicate as the first complaint, but also characterized Delta Dental's conduct as a "group boycott." On July 25, the district court dismissed SmileCare's federal claims with prejudice under Fed. R. Civ. P. 12(b) (6). *SmileCare Dental Group v. Delta Dental Plan of California*, 858 F. Supp. 1035 (C.D. Cal. 1994). SmileCare timely appeals.

## ANALYSIS

Standard of review.

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[1] SmileCare also alleges that Delta Dental's conduct is in violation of Cal. Health & Safety Code § 1371.2, which provides that health service care providers may not:

> reduce the level of payment to a provider based solely on the allegation that the provider has entered into a contract with any other licensed health care service plan for participation in a benefit plan that has been approved by commissioner.

According to SmileCare, the statute "forbids Delta Dental from reducing the level of payments to supplemental plan dentists." Delta Dental responds that its actions were prompted by providers' breach of contract, and not "solely" on their participation in another health care plan. The district court dismissed SmileCare's stat law claims, including the statutory claim, without prejudice. The state law claims are not at issue on appeal.

Dismissal pursuant to Fed R. Civ. P. 12 (b) (6) is reviewed *de novo*. *Everest & Jennings v. AmericanMoterists Ins. Co.*, 23 F.3d 226, 228 (9th Cir. 1994). All allegations of material fact are taken as true and construed in the light most favorable to the plaintiff. *Id.* at 229. A complaint should not be dismissed unless it appears beyond doubt that plaintiff can prove no set of facts in support of his claim which would entitle him to relief. *Id.* The court may dismiss a complaint as a matter of law for "(1) lack of a cognizable legal theory or (2) insufficient facts under a cognizable legal claim." *Robertson v. Dean Witter Reynolds, Inc.*, 749 F.2d 530, 534 (9th Cir. 1984).

[1] Whether specific conduct is anticompetitive is a question of law reviewed *de novo*. *Oahu Gas Serv., Inc. v. Pacific Resources, Inc.*, 838 F. 2d 360, 368 (9th Cir,), *cert. Denied*, 488 U. S. 870 (1988). Dismissal for failure to state a claim is appropriate where "the complaint states no set of facts which, if true, would constitute an antitrust offense, notwithstanding its conclusory language regarding the elimination of competition and improper purpose." *Rutman wine Co. v. E. & J. Gallo Winery*, 829 F.2d 729, 735 (9th Cir. 1987) (quotations and alteration omitted).

## I

Section 2 of the Sherman Act provides: "Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other persons, to monopolize any part of the trade or commerce ... shall be deemed guilty of a felony ..." 15 U.S.C. § 2. "In order to state a claim for monopolization under Section 2 of the Sherman Act, a plaintiff must prove: (1) Possession of monopoly power in the relevant market; (2) willful acquisition or maintenance of that power;

and (3) casual antitrust injury." *Pacific Express, Inc. v. United Airlines, Inc.*, 959 F.2d 814, 817 (9th Cir.), *cert. denied*, 506 U.S. 1034 (1992). The following elements are required to establish an attempt to monopolize claim: "(1) specific intent to control prices or destroy competition; (2) predatory or anti-competitive conduct to accomplish the monopolization; (3) dangerous probability of success; and (4) casual antitrust injury." *Id.* Delta Dental does not dispute SmileCare's allegation that it possesses market power;[2] the remaining issue is whether SmileCare has adequately alleged intentional predatory or anticompetitive conduct and resultant injury.

The briefs of both parties and *amici* devote a great deal of space to evaluating the competitive merits of insurance co-payment plans. However, the legality of co-payment plans and waiver prohibition clauses is neither at issue nor seriously in question. In *Davidowitz v. Delta Dental Plan of California, Inc.*, 946 F.2d 1476, 1479 (9th Cir. 1991), we adopted the Seventh Circuit's reasoning in *Kennedy v. Connecticut Gen. Life Ins. Co.*, 924 F. 2d 698 (7th Cir. 1991), approving an insurer's prohibition on providers' waiver of patient co-payments because "waivers annul the benefits of the co-payment system." 924 F.2d at 699. *Davidowitz* extended *Kennedy* to uphold Delta Dental's non-assignment policy barring beneficiaries from assigning benefits to nonparticipating providers. 946 F.2d at 1481. The non-assignment clause prevented nonparticipating dentists from

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[2] According to the district court, "Delta Dental concedes that SmileCare has adequately alleged market power." SmileCare, 858 F. Supp. at 1037. While the parties do not discuss the issue of market power on appeal, we observe that market share does not necessarily equal market of monopoly power, which further requires an assessment of such factors as ease of entry. United States v. Syufy Enters., 903 F.2d 659, 664 (9th Cir. 1990). See also Ball Memorial Hosp., Inc. V. Mutual Hosp. Ins., 784 F.2d 1325, 1335-37 (7th Cir. 1986) (where there are no barriers to entry, insurer with large market share lacked market power).

asking their patients to assign the dentists their rights to receive Delta Dental's checks, typically in exchange for waiver of the co-payment. *Id.* at 1477 n.1.

[2] Notwithstanding its lengthy forays into the questionable market benefits of insurance co-payment plans, SmileCare repeatedly asserts that it is *not* challenging Delta Dental's co-payment scheme *per se*. Nor is it questioning Delta Dental's right to insist that providers not waive the co-payment. Rather, it is challenging Delta Dental's behavior in refusing to honor supplemental insurers' coverage of the patient's co-payment because it deems such coverage as tantamount to waiver of the co-payment. The key issue, then, is whether Delta Dental's refusal to recognize as contractually valid a participating dentist's acceptance of co-payment from a supplemental insurer rather than from the patient herself has any impermissible anticompetitive effects. *See Barry v. Blue Cross of California*, 805 F.2d 866, 871-72 (9th Cir. 1986).[3]

The district court responded to this question after visiting the merits of co-payment plans themselves. *SmileCare*, 858 F. Supp. at 1038-39. The court opined that insurance creates a "moral hazard" because it desensitizes patients to cost and induces them to seek inordinate amounts of care; co-payments offset this hazard by forcing

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[3] Potential harm to SmileCare alone will not prove SmileCare's case. The courts have repeatedly observed that "the antitrust laws protect competition, not competitors." *United States v. Syufy Enters.*, 903 F.2d 659, 668 (9th Cir. 1990). *See also Ocean State Physicians Health Plan, Inc. v. Blue Cross & Blue Shield of Rhode Island*, 883 F. 2d 1101, 1110 (1st Cir. 1989) ("Section 2 does not prohibit vigorous competition on the part of a monopoly. To the contrary, the primary purpose of the antitrust laws is to encourage competition."), *cert. denied*, 494 U.S. 1027 (1990).

patients to reflect upon the cost of services and moderate their demands for treatment. *Id.* at 1038 (citing *Ball Memorial Hosp., Inc. v. Mutual Hosp. Ins., Inc.*, 784 F.2d 1325, 1332 (7th Cir. 1986), *Kennedy*, 924 F.2d at 699-701, and *Davidowitz*, 946 F.2d at 1479). The district court denied as a matter of law SmileCare's contention that "supplemental plans are not waivers of co-payments, but rather are merely substitutes for them," based on its finding that supplemental plans create the same "moral hazard" as waivers because they render patients insensitive to cost. *Id.* at 1039.

We need not adopt the "moral hazard" theory or reach a conclusion as to the relative market advantage of co-payment plans to decide the instant case. As we stated in *Davidowitz*, "[we are] not called upon to weigh the wisdom or the public policy of payment assignability. That is the function of Congress. We merely hold the non-assignment clause is legal and is not prohibited by Congress." 946 F. 2d at 1481. *See also Kennedy*, 924 F. 2d at 702 ("Whether full indemnity is preferable to a co-payment system is a question for the marketplace. The answer in this health plan is co-payments, and its terms will be enforced.")

The *Kennedy* court explained that,

> [the defendant insurer's] policy require[s] co-payments in order to maintain incentives that hold down the cost of medical care. We could not break the circle in favor of reimbursement without abrogating the co-payment requirement -- a requirement that [defendant] had every legal entitlement to create....If a [provider] wishes to receive

> payment under a plan that requires co-payments, then he must collect those co-payments -- or at least leave the patient legally responsible for them.

*Id.* The court added this instructive note: "[Plaintiff] observes that the patient's rich aunt or best friend may pay the 20% and asks rhetorically: Why can't the doctor pay? The answer is contractual: Because the plan and policy say that the physician must create a legal obligation in the employee or dependent." *Id.*

The same reasoning applies here. Delta Dental concedes that if SmileCare paid the *patient* the co-payment, and the patient then paid the dentist, it would have no objection or cause to find its providers in breach of contract. This would mirror the scenario with the rich aunt. However, because SmileCare pays the *dentist*, the legal obligation required of the insured is eliminated, distorting the actuarial basis for Delta Dental's co-payment plan.[4]

[3] The district court denied as a matter of law SmileCare's argument that "Delta Dental's conduct is anticompetitive because it stamps out supplemental plans," based on its finding that SmileCare's supplemental insurance plan does not compete with

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[4]The actuarial basis for Delta Dental's co-payment plan is premised in the theory that insureds will seek cheaper of less frequent treatment if they are forced to consider the pinch to their own wallets. When SmileCare pays the patient's portion of the fee, the patient has no reason to shop for a less expensive provider or to question the necessity of certain treatments. As the district court observed, "SmileCare and the patient pocket Delta Dental's loss. Of course, this windfall will be short-lived," for Delta Dental will raise its prices or abandon co-payment plans all together as unprofitable. SmileCare, 858 F. Supp. at 1039.

Delta Dental's primary plan. *SmileCare*, 858 F. Supp. at 1039.[5] "Competitive discipline comes not from supplemental plans, but from competing primary plans." *Id.* The court acknowledged that employees already covered through their employers or unions by Delta Dental's mandatory co-payment plan might wish to obtain 100% coverage by purchasing supplemental coverage. "If Delta Dental overcharges for supplemental plans, competitors will induce the patient's employer to switch mandatory co-payment plan providers....As long as Delta Dental does not improperly attempt to crush competition in the primary plan market, it does not act anticompetitively." *Id.* at 1040 (footnotes omitted).

SmileCare maintains that it is competing with Delta Dental because its supplemental plan threatens Delta Dental's business and provides the consumer with a better product at a lower cost. It cites *Syufy* for the proposition that competition exists where parties impose "an essential discipline [on one another] to provide the consumer with a better product at a lower cost." 903 F.2d at 663. However, SmileCare's plan does not put pressure on Delta Dental to reduce the price of its co-payment plan. To the contrary, by eliminating the patient's contribution for each service, the supplemental plan eliminates the anticipated benefit of reduced demand for services. The supplemental plan thus has the potential to increase Delta Dental's costs, pressuring it to raise the cost of co-payment plans or eliminate them altogether, to the ultimate detriment of the consumer.

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[5]The court reasoned that moral hazard and antitrust price-fixing prohibitions require that supplemental and co-payment plans be offered by the same insurer. *See SmileCare*, 858 F. Supp. at 1038-39, 1039 n.3 and 1040 n.5.

[4] Instead of competing with Delta Dental directly, SmileCare would "discipline" Delta Dental by encroaching upon its method of disciplining its insureds. We therefore agree with the district court's conclusion that SmileCare and Delta Dental are not true competitors. Rather, SmileCare has found a niche in the coverage "gap" created by Delta Dental's co-payment plan, and now seeks to impose on Delta Dental its own way of doing business.[6] SmileCare fails to cite any provision under the antitrust laws that would require Delta Dental to modify a legitimate way of doing business in order to allow SmileCare to sell its plan.

[5] Even assuming arguendo that the parties were competitors, SmileCare's claims that Delta Dental's conduct amounted to "group boycott" or "refusal to deal" in violation of the antitrust laws are not persuasive. SmileCare addressed these claims at greater length before the district court than on appeal. There SmileCare argued that "Delta Dental has used its dominant position in the market to coerce or induce third parties -- dentists -- to 'boycott' SmileCare supplemental coverage patients and plans," 858 F.Supp. at 1040, and that "Delta Dental has improperly refused to deal with [SmileCare's supplemental plan]." *Id.* at 1041. SmileCare does not take issue with the court's characterization of its claims.

[6] On appeal, SmileCare cites *Klor's Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1959), and *Aspen Skiing Co. v. Aspen*

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[6] Although the complaint alleges that SmileCare and Delta Dental are competitors, this is a legal conclusion which we are not bound to accept. *Rutman Wine Co. v. E.&J. Gallo Winery*, 829 F.2d 729, 735 (9th Cir. 1987). Accepting as true all of the factual allegations in SmileCare's complaint, appellate brief, and oral argument, we conclude that SmileCare's supplemental plans merely fill a "gap," and therefore do not compete with Delta Dental's primary plans.

*Highlands Skiing Corp.*, 472 U.S. 585 (1985), in support of its group boycott and refusal to deal claims.[7] In *Klor's*, the Supreme Court held that an alleged conspiracy between Broadway-Hale and various manufacturers and distributors to refuse to sell to its competitor, or to sell to it only on unfavorable terms, stated a claim under Sections 1 and 2 of the Sherman Act. 359 U.S. at 209-13. The district court found *Klor's* inapposite because it "only forbade a reseller from coercing suppliers not to sell competing goods to the reseller's competitor," and SmileCare and Delta Dental are not competitors. *SmileCare*, 858 F.Supp. at 1040. Whether or not the parties are in competition, we hold that SmileCare's failure to allege

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[7] The parties also cite *Reazin v. Blue Cross & Blue Shield of Kansas, Inc.*, 899 F.2d 951 (10th Cir.), *cert. denied*, 497 U.S. 1005 (1990), and *Ocean State Physicians Health Plan, Inc. v. Blue Cross & Blue Shield of Rhode Island*, 883 F.2d 1101, 1110 (1st Cir. 1989). SmileCare contends that *Reazin* is "on all fours" with the case at hand; Delta Dental makes the same claim for *Ocean State*.

In *Reazin*, an alleged conspiracy between Blue Cross and two of its participating hospitals to terminate a third hospital's contracting provider agreement and to reduce maximum allowable payments to participating hospitals was deemed an unlawful boycott and refusal to deal. *See* 899 F.2d at 954-55. In *Ocean State*, the court approved Blue Cross's policy of reducing the fee schedules of participating providers who accepted lower fees from a competitor insurance company, holding that even if Blue Cross's application of its policy injured its competitor's business and was in fact *intended* to put its competitor out of business, Blue Cross committed no antitrust violation because the policy itself was legitimate. *Id.* At 1112-13.

Despite superficial similarities to the case before us, the cases cited concern substantially different issues. Both *Reazin* and *Ocean State* involve the propriety of mechanisms designed to control health care costs directly through price agreements (sometimes called "Most Favored Nation" clauses) between insurers and providers. Here, the clause in question is not a price-setting arrangement, but what might be termed a patient-control mechanism. That is to say, the no-waiver provision is designed to control costs by making patients conscious of the price of dental care. It does not control the price of dental services, but rather the frequency with which they are used. Because we find the clause in question significantly different than the ones at issue in the cases cited, we do not consider them in reaching our decision.

the essential element of conspiracy between Delta Dental and any other parties precludes a group boycott claim. *See Klor's*, 359 U.S. at 212.

In *Aspen*, the Supreme Court considered a decision by a ski resort to back out of a ticket-sharing arrangement it had long held with a smaller competitor. The Court held that because the larger resort's decision "to change the character of the market" was not based on efficiency or any other legitimate business reason, its conduct was in violation of Section 2 of the Sherman Act. 472 U.S. at 604-10. We agree with the district court that this case, too, is inapposite. Unlike the defendant skiing company in *Aspen*, Delta Dental did not discontinue a marketing arrangement with SmileCare. Delta Dental's co-payment plan pre-existed SmileCare's supplemental plan and the parties have never co-operated to supply the market with a new or better product. Nor did Delta Dental impose the prohibition against waiver of the co-payment as a response to SmileCare's plan.

[7] Furthermore, as the district court observed, it is well-established that competitors do not have a general duty to deal with one another. *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 483 n.32 ("as a general matter a firm can refuse to deal with its competitors. But such a right is not absolute; it exists only if there are legitimate competitve [sic] reasons for the refusal.") (citing *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 602-605 (1985)); *Oahu*, 838 F.2d at 368 (duty to deal with competitors "arise[s] only when there is no justification for refusing to aid a competitor. "Where a monopolist's refusal to aid a competitor is based partially on a desire to restrict competition, we determine antitrust liability by asking whether there was a legitimate

business justification for the monopolist's conduct.").

[8] While the existence of valid business reasons is ordinarily a question of fact, in the case before us it is a foregone conclusion requiring no further analysis: The validity of Delta Dental's business reasons for requiring its dentists to collect the co-payment directly from the patient has already been established by our decision in *Davidowitz*. We therefore agree with the district court that Delta Dental's policy is supported as a matter of law by a legitimate business justification – its interest in protecting the disciplinary effect of its co-payment plan. *Davidowitz*, 946 F.2d at 1479-81; *see also Kennedy*, 924 F.2d at 699-701.

[9] Because Delta Dental's co-payment plan is concededly legitimate, and because SmileCare has failed to allege that Delta Dental's enforcement of its no-waiver clause has any anticompetitive effects, we affirm the district court.

AFFIRMED.

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PREGERSON, Circuit Judge, dissenting:

Because I believe that certain acts allegedly committed by Delta Dental, if proved, could constitute anticompetitive and predatory conduct within the meaning of the antitrust laws, I dissent.

The majority opinion holds that Delta's conduct forcing SmileCare and other supplemental plans out of the dental insurance market cannot be interpreted as anticompetitive because Delta and

SmileCare are not true competitors and because the business policy by which Delta justifies its allegedly anticompetitive conduct is legitimate. Based on the procedural posture of this appeal, I disagree.

On a motion to dismiss for failure to state a claim under Fed.R.Civ.P. 12(b)(6), facts alleged by the nonmoving party are presumed to be true. *Everest & Jennings v. American Motorists Ins. Co.*, 23 F.3d 226, 228 (9th Cir. 1994). The district court contravened this rule when it made the "finding" -- without any evidence -- that "SmileCare's supplemental insurance plan does not compete with Delta's primary plans." *SmileCare*, 858 F. Supp. at 1039. The majority opinion now erroneously concludes that Delta and SmileCare are not true competitors based solely on the district court's "finding."

Both the district court's finding and the majority opinion's conclusion that Delta Dental's policy results in no impermissible anticompetitive effects rest on cases interpreting ERISA rather than the Sherman Act. *See* maj. op. at 8, 10; *SmileCare*, 858 F. Supp. at 1038-39 (citing *Davidowitz v. Delta Dental Plan of Cal., Inc.*, 946 F.2d 1476, 1479 (9th Cir. 1991) and *Kennedy v. Connecticut Gen. Life Ins. Co.*, 924 F.2d 698 (7th Cir. 1991)). The purpose of ERISA is to protect employee benefits. By contrast, the purpose of the Sherman Act is to protect competition. *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 224 (1993). The issue in *Davidowitz*, whether a non-assignment clause is barred by ERISA, is an entirely different question from the issue in this case. The issue here is whether, under the Sherman Act, Delta Dental's actions in refusing to allow participating dentists to accept a co-payment from a supplemental insurer rather than the patient are lawful.

To decide whether Delta and SmileCare are competitors, the district court must first conduct a factual inquiry into the definition of the relevant market. *See Thurman Industries, Inc. v. Pay 'N Pak Stores, Inc.*, 875 F.2d 1369, 1374 (9th Cir. 1989). Defining the product market involves identification of the field of competition: the group or groups of sellers or producers who have actual or potential ability to deprive each other of significant levels of business. Because a factual inquiry is necessary to determine this issue, *id.*, it was improper for the district court to decide it on a motion to dismiss.

The majority opinion then states that, assuming Delta and SmileCare were competitors, the key question is whether Delta's refusal to accept SmileCare supplemental payments in lieu of patients' co-payments has anticompetitive effects. The majority opinion holds that Delta's conduct is not anticompetitive because Delta has a legitimate business justification for its refusal to accept SmileCare's supplemental payments. This misguided analysis, however, puts the cart before the horse.

A business justification is a defense to allegations of anticompetitive conduct. *Phonetele, Inc. v. American Tel. and Tel.*, 664 F.2d 716, 739 (9th Cir. 1981), *modified*, 1982 WL 11277 (1982), *and cert. denied*, 459 U.S. 1145 (1983). But to reach the business justification issue, a court must first decide whether the conduct is anticompetitive. If the court finds that the conduct is anticompetitive, the defendant must then affirmatively show that there was a valid business reason for the conduct. *Id.* Furthermore, whether a valid business reason justifies a monopolist's conduct is a question of fact. *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 604-05 (1985). It is therefore improper for a court to

decide on a motion to dismiss whether a business justification exists.

In deciding the issue, what the district court has really done is to ignore the rule that on a motion to dismiss facts alleged by the nonmoving party are presumed true. *Everest*, 23 F.3d at 228. Instead of taking as true all of SmileCare's allegations about the anticompetitive effects of Delta's conduct, the district court has turned the standard on its head by taking only Delta's asserted defense as true. It is improper for the court to make such an evaluation of asserted defenses at this stage in the proceedings. In fact, a court should not consider defenses at all on a motion to dismiss. All the court may do is decide whether or not the well-pleaded facts, if proved, could constitute a claim that would entitled the plaintiff to relief. This is where the inquiry should end.

Because SmileCare has alleged facts which, if proved, could entitled it to relief under the antitrust laws, *see Conley v. Gibson*, 355 U.S. 41, 45-46 (1957), this case should have survived a motion to dismiss. I would therefore reverse.

FILED
JUL 25 1994
CLERK, U.S. DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA
BY DEPUTY

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

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| SMILECARE DENTAL GROUP, | NO.CV 93-5437 RG(SHx) |
| Plaintiff, | |
| v. | ORDER GRANTING DEFENDANT'S |
| DELTA DENTAL PLAN OF CALIFORNIA, | MOTION TO DISMISS |
| Defendant. | |

I. Background

Plaintiff SmileCare Dental Group ("SmileCare"), and defendant Delta Dental Plan of California ("Delta Dental") offer dental health care plans to employers, labor unions, and individuals. According to SmileCare's complaint, Delta Dental sells plans to 60% of all persons with dental coverage, and has enrolled approximately 95% of California dentists as Delta Dental service providers. FAC. ¶¶ 5-6. Delta Dental directly reimburses dentists for services they provide to patients, but under most plans, pays only a portion of the dentist's fee. The patient is responsible for the remainder, called a "co-payment." By contract, Delta Dental dentists promise to collect the co-payments from the patients. FAC. ¶ 8.

Plaintiff SmileCare offers a supplemental dental plan called

"SmileCare Coverage Plus." SmileCare sells Coverage Plus to patients already covered by dental plans which provide less than 100% coverage, including those covered by Delta Dental's primary plans. FAC. ¶ 9. Since Coverage Plus pays the patient's co-payment, patients with both Coverage Plus and Delta Dental insurance have 100% coverage.

SmileCare contends that Delta Dental has taken a variety of improper actions designed to eliminate SmileCare's Coverage Plus plan. For example, Delta Dental informs dentists who accept co-payments from Coverage Plus that they have breached their contract with Delta Dental by waiving the co-payment. FAC. ¶ 11. Consequently, Delta Dental, "by some unspecified, mystical calculation, recompute[s] the provider's fee schedule and [pays] the dentist a vastly reduced, non-compensatory sum for the services performed." FAC. ¶ 11. Moreover, Delta Dental allegedly has both threatened and terminated Delta providers who accept SmileCare Coverage Plus co-payments. FAC. ¶ 12.

According to SmileCare, Delta Dental's conduct "denies patients access to the dentist of their choice and to expanded SmileCare services," and "prevents SmileCare from being able to effectively compete in the California dental health plan market [by] produc[ing] a boycott by Delta providers of patients having SmileCare supplemental dental health coverage." FAC. ¶ 20.

SmileCare filed suit, alleging a Sherman Act Section 2 claim and several supplemental state law claims, including tortious interference, trade libel, breach of contract, and violations of the California Health and Safety Code and California Business and Professions Code. On January 24, 1994, Delta Dental moved to dismiss under F.R.Civ.P. 12(b)(6), arguing that SmileCare had not alleged anticompetitive conduct and therefore failed to state a

Sherman Act Section 2 claim. This Court agreed, and dismissed SmileCare's complaint without prejudice. After SmileCare filed a first amended complaint, Delta Dental moved to dismiss on the same grounds.[1]

II. Standard for Motion to Dismiss

In general, courts may dismiss a complaint under Fed.R.Civ.P. 12(b)(6) only if "no relief could be granted under any set of facts that could be proved consistent with the allegations." See, e.g., Hishon v. King & Spalding, 467 U.S. 69, 73 (1984). When evaluating a Rule 12(b)(6) motion, courts must presume that all factual allegations are true and draw all reasonable inferences in favor of the non-moving party. Western Concrete Structures Co. v. Mitsui & Co., 760 F.2d 1013, 1015 (9th Cir.), cert. denied, 474 U.S. 903 (1985); Kennedy v. H & M Landing, Inc., 529 F.2d 987, 989 (9th Cir. 1976).

As SmileCare notes, "summary dismissals of antitrust actions are disfavored." Western Concrete Structures, 760 F.2d at 1016. However, whether specific conduct is anticompetitive is a question of law. Oahu Gas Service, Inc. v. Pacific Resources, Inc., 838 F.2d 360, 368 (9th Cir.), cert. denied, 488 U.S. 870 (1988); Rutman Wine Co. v. E. & J. Gallo Winery, 829 F.2d 729, 735-36 (9th Cir. 1987). Therefore, courts should evaluate allegations of anticompetitive conduct at the F.R.Civ.P. 12(b)(6) stage, and dismiss complaints if they "state[] no set of facts which, if true, would constitute an antitrust offense, notwithstanding [their] conclusory language regarding the elimination of competition and improper purpose."

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[1] This Court has jurisdiction over SmileCare's Sherman Act claim under 28 U.S.C. § 1331 and supplemental jurisdiction over the state law claims under 28 U.S.C. § 1367.

Rutman Wine, 829 F.2d at 735. In such cases, Rule 12(b)(6) dismissal "especially makes sense because the costs of discovery in [antitrust] actions are prohibitive." Id. at 738.

III. SmileCare's Sherman Act Claim

Under Sherman Act Section 2, a monopolization claim must allege (1) possession of monopoly power in the relevant geographic and product markets; (2) willful acquisition or maintenance of that power; and (3) antitrust injury. Pacific Express, Inc. v. United Airlines, Inc., 959 F.2d 814, 817 (9th Cir.), cert. denied, 113 S. Ct. 814 (1992). An attempt to monopolize claim must allege (1) specific intent to control prices or destroy competition; (2) predatory or anticompetitive conduct; (3) a dangerous probability of success; and (4) causal antitrust injury. Id. For purposes of this motion, Delta Dental concedes that SmileCare has adequately alleged market power. However, Delta Dental contends that SmileCare fails to allege the requisite anticompetitive conduct. See Western Concrete Structures, 760 F.2d at 1017-18 ("[A]ttempt to monopolize and actual monopolization involve, among other things, intentional predatory or anticompetitive conduct."). See also United States v. Grinnell Corp., 384 U.S. 563, 570-71 (1966) (stating that market power obtained or preserved "as a consequence of a superior product, business acumen, or historic accident," is not condemned by the antitrust laws); United States v. Syufy Enters., 903 F.2d 659, 668-69 (9th Cir. 1990); Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263, 273-75 (2d Cir. 1979), cert. denied, 444 U.S. 1093 (1980).

a. Anticompetitive Conduct

SmileCare concedes that Delta Dental's patient co-payment requirement is unobjectionable. Delta Dental argues that once one

makes that concession, one must also concede that enforcing the co-payment requirement is not anticompetitive.

This Court agrees with Delta Dental. Mandatory co-payment plans require patients to pay their co-payments themselves, thereby precluding them from obtaining supplemental insurance. However, mandatory co-payment plans are no more inherently anticompetitive than 100% plans or any other ordinary buyer/seller arrangement. Merely agreeing to be a patient's exclusive dental insurer is not, in and of itself, anticompetitive:

> [E]very contract between a buyer and seller has precisely the effect of which [plaintiff] complains. When a buyer contracts with one seller, a second seller no longer has access to the buyer's business to the extent it is covered by their existing contract. This consequence, however, is not unlawful. The [plaintiffs] have confused an agreement to boycott with an agreement to buy and sell services.

Barry v. Blue Cross of California, 805 F.2d 866, 871 (9th Cir. 1986) (citations omitted).[2]

In fact, both the Ninth and Seventh Circuits have recognized that enforcement of contractual mandatory co-payment provisions is pro-competitive, because insurance creates a "moral hazard" by making a patient insensitive to cost:

Once a person has insurance, he wants the best care

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[2] The Barry plaintiffs, two physicians who were not Blue Cross providers, "argue[d] that the [Blue Cross] Plan has the consequence of boycotting or shutting out nonparticipating physicians by interfering with their access to patients insured by the Plan." 805 F.2d at 871. Nevertheless, Judge Ideman granted summary judgment for Blue Cross, and the Ninth Circuit affirmed, concluding that Blue Cross's actions were not anticompetitive.

> regardless of cost -- for someone else bears the cost. When, as happens often, the physician rather than the patient makes the important choices, the physician may be inclined to provide all the service for which insurance will pay, knowing that his patient will not resist his recommendation (at least not on account of expense). Yet if every physician supplies more or better care, price must rise, which patients as a group must pay in higher insurance bills.

Ball Memorial Hospital, Inc. v. Mutual Hospital Ins., Inc., 784 F.2d 1325, 1332 (7th Cir. 1986). Mandatory co-payments combat this effect:

> Co-payments sensitize [patients] to the costs of health care, leading them not only to use less but also to seek out providers with lower fees . . . which makes medical insurance less expensive and enables employers [and health care plan providers] to furnish broader coverage. . . . [I]f waiver of co-payments is allowed, [or if the patient does not have to make the payment herself] patients prefer the lower outlays but waivers annul the benefits of the co-payment system. The health insurer wants assurance that the patient has given enough thought to the need for [and price of] this medical care to be willing to pay. Patients who pay nothing have no reason to moderate their demands for medical service, and providers may inflate the bill.

Davidowitz v. Delta Dental Plan of California, Inc., 946 F.2d 1476, 1479 (9th Cir. 1991) (quoting Kennedy v. Connecticut General Life Ins. Co., 924 F.2d 698, 699-701 (7th Cir. 1991)). See also Westchester Radiological Assocs. P.C. v. Empire Blue Cross and

Blue Shield, Inc., 707 F. Supp. 708, 710 (S.D.N.Y.), aff'd, 884 F.2d 707 (2d Cir. 1989), cert. denied, 493 U.S. 1095 (1990). Thus, an insurer's efforts to force providers to honor their mandatory co-payment contracts increase the array of dental plans by making mandatory co-payment plans feasible, thereby giving consumers broader choice, reducing insurance costs, and enabling employers to furnish broader coverage. Kennedy v. Connecticut General Life Ins. Co., 924 F.2d 698, 699 (7th Cir. 1991).

A simple example, which this Court provided in its previous order, illustrates the principles described by Davidowitz, Ball Memorial Hospital, and Kennedy. Suppose that Delta Dental expects to pay providers $250 per year for treating a patient who is 100% covered. Ignoring administrative costs and overhead, Delta Dental must charge at least $250 to break even. Suppose also that Delta Dental discovers that due to the moral hazard, this patient would seek less dental care, say, $200 per year, if he is forced to make a 20% co-payment himself. Under this 20% co-payment plan, Delta Dental would pay providers only $160 per year. Now suppose this patient, covered by Delta Dental's 20% co-payment plan, purchases a Coverage Plus plan from SmileCare, which agrees to pay his co-payments. This patient, who would have sought only $200 in dental care without Coverage Plus, is now no longer deterred by co-payments. Consequently, he seeks $250 in dental care, forcing Delta Dental to pay providers $200 per year, $40 more than it expected. SmileCare and the patient pocket Delta Dental's loss. Of course, this windfall will be short-lived: Unless Delta Dental is allowed to treat supplemental plan payments as impermissible waivers of patient co-payments, it will soon abandon mandatory co-payment plans as

unprofitable.[3]

SmileCare acknowledges the moral hazard,[4] and does not ask this Court to repudiate Davidowitz, Ball Memorial Hospital, and Kennedy. Instead, SmileCare argues that supplemental plans are not waivers of co-payments, but rather are merely substitutes for them. Such a distinction is incorrect as a matter of law. So long as a patient is not making the co-payments himself, he is desensitized to cost,

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[3] The mandatory co-payment/supplemental plan combination is inherently unstable unless the primary plan provider and the supplemental plan provider collude. Suppose, in the example previously discussed, that Delta Dental is forced to accept payments from SmileCare supplemental plan payments as valid co-payments. Delta Dental will either cease offering the mandatory co-payment plans or increase its price. Delta Dental will have to charge $200 to ensure that it will break even if a patient purchases SmileCare's supplemental coverage. Of course, this renders the mandatory co-payment plan uneconomical for patients who do not wish to purchase supplemental plan coverage (these patients would pay $200 for the Delta Dental plan, plus $20 in co-payments, and receive only $200 in services). Thus, insurers can offer supplemental plans which complement another insurer's mandatory co-payment plan only if the insurers agree to split the cost such that neither operates at a loss.

Although such communication would allow complementary supplemental and mandatory co-payment plans to be offered by different plan provider, it would not have any salutary effect. Complementary supplemental plans can be provided by the same company offering the mandatory co-payment plan – without incurring the additional transactions costs necessary if two different companies offer the complementary plans. Moreover, such communication would have a potentially disastrous effect on the primary plan market, in which Delta Dental and SmileCare compete, by needlessly facilitating price discussions between competitors in the primary plan market. See generally United States v. Container Corp. of America, 393 U.S. 333 (1969); America Column & Lumber Co. v. United States, 257 U.S. 377 (1932); Maple Flooring Mfrs. Ass'n v. United States, 268 U.S. 563 (1925).

[4] Both the initial complaint and the first amended complaint concede that if patients have to make co-payments themselves, they will seek fewer dental services. FAC. ¶¶ 17, 22a.; CM. ¶ 9.

even though he must pay a premium for the supplemental insurance.

SmileCare also argues that Delta Dental's conduct is anticompetitive because it stamps out supplemental plans. Specifically, SmileCare argues that, if Delta Dental did not "act anticompetitively," patients could obtain 100% coverage by purchasing either (1) a Delta Dental plan with 100% coverage or (2) a Delta Dental co-payment plan and a SmileCare supplemental plan. SmileCare contends that these two options would compete with each other, thereby reducing the price of 100% coverage and increasing output of dental services. By refusing to regard supplemental plan payments as valid co-payments, Delta Dental allegedly insulates itself from this competition.

This theory is also incorrect as a matter of law. SmileCare misunderstands the very definition of competitor -- Delta Dental does not compete with itself. SmileCare cannot seriously suggest that Delta Dental will cut the price of its 100% plan solely to compete with Delta Dental's mandatory co-payment plan. Absent competition from other primary plans, Delta Dental would simply set the price of both plans at monopolistic levels.

Competitive discipline comes not from supplemental plans, but from competing primary plans. Certainly, some employees may already have a Delta Dental mandatory co-payment plan through their employers or labor unions and wish to purchase supplemental coverage so they can be 100% covered. If Delta Dental overcharges for supplemental plans, competitors will induce the patient's employer to switch mandatory co-payment plan providers by promising to charge lower rates to employees who seek supplemental coverage. As long as Delta Dental does not improperly attempt to crush

competition in the primary plan market,[5] it does not act anticompetitively.[6]

Thus, this Court finds that SmileCare's First Amended Complaint fails to state a Sherman Act claim. A few additional remarks are warranted, however, regarding the boycott and refusal to deal cases upon which SmileCare relies.

b. "Induced Boycott" -- Klor's v. Broadway-Hale

SmileCare contends that Klor's, Inc. v. Broadway-Hale Stores, Inc., 359 U.S. 207 (1959) supports its claim that Delta Dental has used its dominant position in the market to coerce or induce third parties -- dentists -- to "boycott" SmileCare supplemental coverage patients and plans. In Klor's, plaintiff, Klor's, Inc., and defendant,

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[5] One cannot speak in terms of an independent supplemental plan "market," because the moral hazard requires supplemental plans and mandatory co-payment plans to be offered by the same insurer. Thus, SmileCare cannot, as a matter of law, complain that the supplemental plan market is not competitive. As discussed above, competition in the primary plan market keeps health insurance prices, including those for supplemental plans, at a competitive level.

[6] Since SmileCare fails to allege anticompetitive conduct, it also fails to allege antitrust injury. SmileCare alleges that Delta Dental terminates dentists who accept co-payments from SmileCare's coverage plus plan, but Delta Dental does not allegedly tell dentists that they cannot be providers for SmileCare primary plans if they want to be Delta Dental providers. While the terminations might harm the dentists, they do not give rise to antitrust injury to SmileCare. So long as no entry barriers preclude SmileCare from competing in primary plan market (and SmileCare has alleged none), Delta Dental's alleged practice of terminating dentists who accept co-payments from SmileCare could be expected to benefit SmileCare, since patients wishing to continue treatment from these dentists would be encouraged to switch to SmileCare primary plans. Certainly, some patients might choose to switch dentists instead of dental health care plans, but their decision would harm dentists -- not SmileCare.

Broadway-Hale, were adjacent retail stores in San Francisco which sold similar household appliances. Broadway-Hale ran local newspaper ads showing its products and prices. Klor's took copies of these ads, marked down the prices, and posted them in its own windows, thereby luring customers away from Broadway-Hale. In an attempt to stop this practice, Broadway-Hale allegedly convinced several appliance manufacturers and distributors to sell to Klor's only on highly unfavorable terms, if at all. Klor's sued, alleging claims under Sherman Act Sections 1 and 2.

The Supreme Court held that Klor's had successfully alleged Section 1 and 2 violations, remarking that the alleged conspiracy "takes from Klor's its freedom to buy appliances in an open competitive market and drives it out of business as a dealer in defendants' products." Klor's, 359 U.S. at 213. However, Klor's did not forbid Broadway-Hale from acting to enforce pro-competitive contracts with Broadway-Hale. Rather, Klor's only forbade a reseller from coercing suppliers not to sell competing goods to the reseller's competitor. Because supplemental plans do not provide competitive pressures -- an insurer does not compete with itself -- SmileCare does not state a claim under Klor's.[7]

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[7] Similarly, SmileCare does not state a claim under Reazin v. Blue Cross & Blue Shield of Kansas, Inc., 899 F.2d 951 (10th Cir.), cert. denied, 497 U.S. 1005 (1990). Blue Cross, which insured approximately 60% of all Kansas residents, 899 F.2d at 969, terminated its provider contract with a hospital in order to "send a message" to hospitals to boycott Blue Cross' competitors. Id. at 954. The jury found for plaintiffs, and the Tenth Circuit affirmed. Reazin differs little from Klor's – it only forbids a reseller with market power from announcing to a supplier that it cannot sell competing goods to a competing reseller.

Finally, SmileCare also cites Blue Shield of Virginia v. McCready, 457 U.S. 465 (1982). Plaintiff McCready, a Blue Shield subscriber, challenged Blue Shield's practice of unfavorably restricting reimbursement for psychotherapy provided by

c. "Refusal to Deal" -- Aspen Skiing v. Aspen Highlands Skiing

SmileCare relies on Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985), arguing that Delta Dental has improperly refused to deal with the Coverage Plus Plan. Refusal to deal can constitute a Section 2 violation, but only in narrow circumstances. Competitors do not generally have a duty to deal with each other. Eastman Kodak Co. v. Image Tech. Servs., Inc., 112 S.Ct. 2072, 2090 (1992); Aspen Skiing, 472 U.S. at 600; High Technology Careers v. San Jose Mercury News, 996 F.2d 987, 990 (9th Cir. 1993). Ordinarily, to prevent horizontal price fixing and collusion, the antitrust laws discourage unnecessary communication between true competitors. See generally United States v. Container Corp. of America, 393 U.S. 333 (1969); American Column & Lumber Co. v. United States, 257 U.S. 377 (1932); Maple Flooring Mfrs. Ass'n v. United States, 268 U.S. 563 (1925). Nevertheless, competitors working together may be able to create a new product which neither could offer on their own. In such cases, the combination should be encouraged, so long as it does not lead the competitors to abuse the opportunity and fix prices on their competing goods. Thus, if competitors combine to create a new product, and one of them backs out without legitimate business reasons for doing so, it may violate

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psychologists as compared to psychiatrists. Id. at 468. By a 5-4 majority, the Supreme Court found that McCready had standing to sue Blue Shield for its "concerted refusal to pay . . . motivated by a desire to deprive psychologists of the patronage of Blue Shield subscribers." Id. at 479. However, because McCready is a standing case, it does not speak in detail of the substance of plaintiff's antitrust claims. This Court declines to read McCready as suggesting that absent entry barriers or anticompetitive conduct, resellers must purchase from all available suppliers. Such an absurd reading would render vertical integration, which is usually pro-competitive, illegal.

Sherman Act Section 2. Aspen Skiing, 472 U.S. at 604-05; City of Anaheim v. Southern California Edison Co., 955 F.2d 1373, 1379 (9th Cir. 1992).

For example, the Aspen Skiing litigants, both ski resorts, combined to sell the "all-Aspen" ski pass, a new and superior product. Aspen Skiing, 472 U.S. at 605-10. The all-Aspen ticket provided skiers with greater and more convenient access to ski services, and thus was a new and different product which could only be offered by the two resorts in combination. Id. Although the all-Aspen ski pass was successful, one of the resorts chose to abandon it, and refused to sell ski passes to the other. The Supreme Court held that the refusal, for which defendant had no justifiable business reason, violated Sherman Act Section 2.

SmileCare's position is only superficially similar to the Aspen Skiing plaintiff's. SmileCare's Coverage Plus and Delta Dental's co-payment plans appear to be complementary -- when combined, the two plans form a new product, 100% coverage. However, nothing makes this new product special, improved, or even different from a 100% plan offered by a single dental insurer. In fact, considering the added administrative and transaction costs of participating in two dental plans, a single 100% plan seems superior. Moreover, unlike the defendant in Aspen Skiing, Delta Dental has valid business reasons for refusing to deal, established by Davidowitz, Ball Memorial Hospital, and Kennedy. Since SmileCare fails to allege that the market gains a new product when a SmileCare supplemental plan and a Delta Dental mandatory co-payment plan are combined, and since Delta Dental has pro-competitive reasons for refusing to deal, SmileCare's Aspen Skiing theory fails.

d. Dismissal With Prejudice.

In its previous order, this Court informed SmileCare that absent an allegation of an anticompetitive practice or entry barrier, SmileCare's contentions that Delta Dental artificially increases prices makes no sense -- so long as others (such as SmileCare) are free to enter the market, prices will remain at a competitive level. SmileCare's amended complaint fails to make any such allegations. Nevertheless, SmileCare argues that it should be given an opportunity to conduct discovery. Absent an allegation of anticompetitive conduct, this Court cannot imagine what this endeavor might prove.

"[R]epeating [a] mantra" of familiar antitrust terms does not immunize SmileCare's complaint from attack. Eastman Kodak, 112 S. Ct. at 2084-85 n.18. See also Rutman Wine, 829 F.2d at 736 ("[I]f the facts [alleged] do not at least outline or adumbrate a violation of the Sherman Act, the plaintiffs will get nowhere merely by dressing them up in the language of antitrust."). Nor does it justify allowing SmileCare to embark upon an expensive fishing expedition, which in and of itself might discourage insurers from offering pro-competitive, mandatory co-payment plans. See Rutman Wine, 829 F.2d at 738 (noting that Rule 12(b)(6) dismissal "especially makes sense because the costs of discovery in [antitrust] actions are prohibitive."); Joseph E. Seagram & Sons, Inc. v. Hawaiian Oke and Liquors, Ltd., 416 F.2d 71, 79 (9th Cir. 1969), cert. denied, 396 U.S. 1062 (1970) (quoting Cardozo, Mr. Justice Holmes, 44 Harv. L. Rev. 682, 688 (1931)) (warning courts to "guard against 'the tyranny of tags and tickets'" -- the temptation to immediately embrace a plaintiff's rote recitation of antitrust terms). This Court has already given SmileCare guidance and an opportunity to amend its complaint. Since

SmileCare fails to allege any anticompetitive conduct, its Sherman Act Section 2 claim is hereby DISMISSED WITH PREJUDICE.

IV. SmileCare's State Law Claims.

SmileCare's remaining claims, for tortious interference, trade libel, breach of contract, and violations of the California Health and Safety Code and California Business and Professions Code, are state law claims. Since this Court only has supplemental jurisdiction over these claims, and since this Court believes that these claims would be resolved most efficiently in a state court, SmileCare's state law claims are hereby DISMISSED WITHOUT PREJUDICE. 28 U.S.C. § 1367(c)(3); Levald, Inc. v. City of Palm Desert, 998 F.2d 680, 692 (9th Cir. 1993), cert. denied, 114 S.Ct. 924 (1994).

IT IS SO ORDERED.

DATED: July 25, 1994

s/Richard A. Gadbois, Jr.
RICHARD A. GADBOIS, JR.
United States District Judge

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FILED
CLERK OF THE COURT
FEB 25 1994
CENTRAL DIST. OF CAL.
BY DEPUTY

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

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| SMILECARE DENTAL GROUP, Plaintiff, vs. DELTA DENTAL PLAN OF CALIFORNIA, Defendant. | CV 93-5437 RG (SHx)<br><br>FIRST AMENDED COMPLAINT FOR DAMAGES AND EQUITABLE RELIEF<br><br>1. Sherman Act<br>2. California Health & Safety Code<br>3. Tortious Interference<br>4. Trade Libel<br>5. California Business & Professions Code<br>6. Breach of Contract<br><br>(DEMAND FOR JURY TRIAL) |

The above-named plaintiff files this complaint against the

above-named defendant and, demanding trial by jury, complains and alleges as follows:

COUNT ONE

(Sherman Act § 2)

I.

JURISDICTION AND VENUE

1. Count One of this Complaint is filed and these proceedings are instituted against the above-named defendant under Sections 4 and 16 of the Clayton Act (15 U.S.C. §§ 15, 26) to secure damages from, and equitable relief against, the above-named defendant for its violations of Section 2 of the Sherman Act (15 U.S.C. § 2).

2. The defendant transacts business, maintains offices and may be found within the Central District of California. The interstate trade and commerce involved and affected by the violation of the antitrust laws alleged herein was carried on in part within this District and some of the unlawful acts described herein were conceived, performed or made effective within this District.

II.

THE PARTIES

3. Plaintiff, SMILECARE DENTAL GROUP ("SMILECARE"), is a corporation organized and existing under the provisions of the Knox-Keene Health Care Service Plan Act of 1975 (California Health & Safety Code § 1340 et seq.) with its principal place of business in Torrance, California and Irvine, California. SMILECARE is engaged in the business of providing both primary and supplemental dental health plans to employers, labor unions and directly to consumers. SMILECARE competes with defendant DELTA DENTAL PLAN OF CALIFORNIA.

4. Defendant, DELTA DENTAL PLAN OF CALIFORNIA

("DELTA"), is a corporation organized and existing under the provisions of the Knox-Keene Health Care Service Plan Act of 1975 with its principal place of business in San Francisco, California. DELTA is engaged in the business of providing dental health plans to employers, labor unions and others. DELTA dominates that business, accounting for about 60% of all persons in California having dental health plan coverage.

III.

NATURE OF TRADE AND COMMERCE

5. Dental health plans have become, over the past decade, an important component of health care coverage provided by employers to employees and, in some instances, by labor unions to their members. DELTA has been and is the dominant provider of dental health plans to employers in the State of California, accounting for about 60% of all employees having employer-provided dental health coverage. DELTA advertises that one of every three persons in California is covered by a DELTA plan.

6. Because of its dominant position in providing dental health plans to employers/employees in California, approximately 95% of the dentists in California are DELTA "providers" of dental services under DELTA dental health plans. It is virtually impossible for a dentist to provide dental services without being a DELTA provider because of the overwhelming number of persons covered by DELTA dental health plans. Thus, DELTA's market power enables it not only to sign up almost all dentists as providers but also to make these dentists dependent on inclusion within DELTA's dental health plans for patients.

7. DELTA does not establish its own fee schedules for "provider" dentists. Rather, DELTA, in its sole discretion, approves a fee schedule, on a line-item-by-line-item basis, provided by each

provider.

8. The vast majority of DELTA dental health plans in California provide for patient "co-payments." Under this arrangement, DELTA agrees to pay the provider a defined percentage of that fee schedule for services performed under a DELTA dental plan. The DELTA provider dentist is contractually obligated to collect from the patient a defined portion of the total charge (the "co-payment"). The amount of co-payment depends on the nature of the treatment. The provider is contractually prohibited from waiving this patient co-payment charge.

9. Although it offers primary dental health plans, SMILECARE is primarily in the business of supplemental dental health plans, which cover the patient co-payment portion of the dental bill. SMILECARE's principal supplemental plan is known as "Smilecare Coverage Plus." The California Department of Corporations, the regulatory agency for Knox-Keene Health Care Plan providers, has reviewed and approved the actuarial soundness of SMILECARE's supplemental dental health plans. SMILECARE offers its supplemental dental health plans to (a) employers, as part of the employee health benefit package; (b) labor unions; and (c) consumers directly at SMILECARE corporate and dental offices.

10. SMILECARE has a group of provider dentists, many of whom are associated with SMILECARE by contract. At DELTA's insistence, all SMILECARE providers who furnish dental services under a DELTA dental health plan must submit dental bills to DELTA through Dr. Hardin, an employee of SMILECARE. Dr. Hardin is the dental director of SMILECARE and, in that capacity, submits bills to DELTA on behalf of all SMILECARE providers.

11. To eliminate competition from SMILECARE, DELTA initially took the position that a DELTA provider who submitted bills

for a patient treated under the SMILECARE Coverage Plus plan had "waived" the patient co-payment and thereby was in breach of the provider agreement with DELTA. DELTA, by some unspecified, mystical calculation, recomputed the provider's fee schedule and paid the dentist a vastly reduced, non-compensatory sum for the services performed. DELTA's conduct directly contravenes Section 1371.2 of California's Health & Safety Code, which provides that no health care plan my reduce the level of reimbursement to a provider (i.e., dentist) based solely on the fact that the provider also contracts with a supplemental plan that, like SMILECARE, is approved by the commissioner.

12. More recently, DELTA adopted a new strategy. DELTA has threatened and has actually terminated DELTA providers who are also SMILECARE dentists.

13. DELTA has articulated that the basis for its conduct is that SMILECARE's supplemental plans are not actuarily sound. DELTA's rationale is a pretext and in bad faith. The California Department of Corporation, the regulatory agency, reached the opposite conclusion. SMILECARE's supplemental dental plans are actuarily sound.

14. DELTA's conduct is intended to, and does, induce dentist providers to refuse to perform services for patients under a SMILECARE supplemental dental health plan. DELTA does so by terminating providers who perform services for a patient who has purchased a SMILECARE supplemental dental plan and/or refusing to reimburse DELTA providers who are also SMILECARE dentists pursuant to the provider agreement.

15. DELTA's conduct is calculated to eliminate SMILECARE's supplemental dental plans from the marketplace and insulate DELTA from competition.

16. Since January 1993, the effective date of California Health & Safety Code § 1371.2, DELTA has paid discriminatory, non-compensatory fees to DELTA providers who also perform services under a SMILECARE supplemental dental plan in direct contravention of that statute, which prohibits such discrimination. Upon information and belief, the California Department of Corporations has sent notice to DELTA that it is in violation of Section 1371.2.

17. The conduct alleged in this Count One directly involves, and substantially and adversely affects, interstate trade and commerce in two separate, but related lines of commerce. First, DELTA providers perform fewer services than would be the case if DELTA permitted them to provide services to patients under SMILECARE's "Coverage Plus." As a consequence, there is a direct restraint upon the tools, equipment, supplies and myriad of commodities which are imported from states other than California and from foreign countries, and which are integrally and essentially involved in providing dental services to California patients. Second, dental health plans involve payments made by out-of-state based employers to DELTA and SMILECARE. Accordingly, DELTA's activities as described herein have actually adversely affected and restrained interstate and foreign commerce and, unless enjoined by this Court, threaten to continue to have such adverse effects upon interstate and foreign commerce.

IV.

VIOLATION ALLEGED

18. Beginning as early as 1989 and continuing up to the time of the filing of this complaint, DELTA has unlawfully acquired and unlawfully maintained a monopoly in, and has unlawfully attempted to monopolize, the business of providing dental health care plans to employers and others in the State of California.

19. In furtherance of its monopolization and attempted monopolization of the relevant market, DELTA has committed the following anticompetitive acts, among others:

a. DELTA has threatened and has actually terminated DELTA providers who also provide dental services under a SMILECARE supplemental dental plan.

b. DELTA has refused to honor approved fee schedules for DELTA providers who provide professional services to patients under SMILECARE's supplemental plan in satisfaction of their "co-payment" requirement. In so doing, DELTA is in direct contravention of California Health & Safety Code § 1371.2.

c. DELTA has refused to recognize the California Department of Corporation's certification of SMILECARE's "Coverage Plus" as a Knox-Keene approved supplemental health care plan.

20. DELTA's conduct has had a least the following anticompetitive effects:

a. DELTA denies patients access to the dentist of their choice and to expanded SMILECARE services such as periodontal care.

b. DELTA prevents SMILECARE from being able to effectively compete in the California dental health plan market in that DELTA's tactics have produced and, unless enjoined, will continue to produce a boycott by DELTA providers of patients having SMILECARE supplemental dental health coverage. DELTA has consciously and deliberately organized a group boycott for the anticompetitive purpose of achieving and/or preserving its dominant market position.

21. No federal or state law or regulatory relationship immunizes, authorizes or condones DELTA's brazen refusal to obey

the law and honor its commitment to DELTA providers who perform services for SMILECARE "Coverage Plus" patients.

V.

EFFECTS OF THE VIOLATIONS

22. The violation of Section 2 of the Sherman Act alleged herein has had, is continuing to have, and unless restrained by this Court, will continue to have the following effects:

a. Consumers have been deprived of the benefits of competition and, as a result of DELTA's unlawful acquisition and unlawful maintenance of monopoly power, have been prevented from securing full and complete dental care protection and have suffered a reduction in the services and an increase in patient cost for services under existing dental plans;

b. DELTA has been and will be able to achieve, or illegally maintain, its monopoly in the provision of dental health care service plans in California;

c. DELTA has been and will continue to terminate DELTA providers who also provide services under a SMILECARE supplemental dental health plan;

d. Dentist providers, and SMILECARE, will continue to receive discriminatory, non-compensatory payment for services rendered when performing such services on a SMILECARE "Coverage Plus" patient;

e. Prices for dental health care plans has been and will continue to be artificially increased and DELTA has been and will continue to be able to exact monopoly profits; and

f. Consumers have had to pay arbitrary and unreasonable co-payment charges and have suffered a depravation of needed dental care.

VI.

INJURY TO PLAINTIFF

23. As a direct and proximate result for the violations alleged herein, plaintiff is and will continue to be irreparably injured in its business and property by defendant's continuing violations. DELTA's conduct, as described above, has reduced the vigor of the competitive process and of competition in the business of providing dental health plans in the State of California. Owing to and as a direct result of that reduction in competition, plaintiff has suffered an inability to compete, a loss of revenues, a loss of substantial goodwill normally attached to a profitable enterprise, and a reduction in the value of its business as a going concern.

24. As a direct and proximate result of the violations alleged herein and as intended by defendant DELTA, plaintiff has sustained injury to its business and property, as follows:

a. it has incurred substantial expenses it would not otherwise have incurred;

b. it has lost revenues it would not otherwise have earned;

c. it has lost profits it would have otherwise made;

d. its ability to raise capital, expand and grow its business has been seriously restrained and suppressed;

e. it has sustained operating losses it would otherwise have avoided;

f. it has lost substantial goodwill and going concern value which would otherwise have attached to it as a profitable enterprise.

25. Plaintiff cannot now measure these damages with specificity. However, plaintiff has reason to believe, in good faith, that these damages exceed $10,000,000. When plaintiff has sufficient information to permit it to allege the quantum of its

damages with specificity, plaintiff will ask leave of Court to amend its complaint to insert said amount herein.

COUNT TWO

(California Health & Safety Code)

26. Count Two of this Complaint is based on supplemental jurisdiction in that the claim asserted herein in ancillary to the federal claim set out in Count One and arises from the same transactions and from a common nucleus of operative facts as alleged in Count One.

27. Count Two of this Complaint is based on Section 1371.2 of the Health and Safety Code of the State of California and seeks damages for DELTA's failure to abide the provisions of that statute since its effective date of January 1, 1993.

28. Plaintiff repeats and realleges the allegations of paragraphs 2-25, inclusive, of Count One of this Complaint with the same force and effect as though each of said paragraphs had been set forth in full herein as part of this Count Two.

29. In direct contravention of Section 1371.2 of the Health and Safety Code of the State of California, DELTA continues to pay providers reduced levels of payment for dental care provided to patients with SMILECARE's Coverage Plus.

30. Despite the plain wording of this statute and despite repeated advice from the Department of Corporations that its conduct violated the statute, DELTA persists, in brazen disregard of the statute, arrogating to itself the right to overrule the Commissioner's finding that SMILECARE's supplemental plan (Coverage Plus) was actuarily sound.

COUNT THREE

(Tortious Interference with Contractual Relations and Prospective Business Advantage)

31. Count Three of this Complaint is based on supplemental

jurisdiction in that the claim asserted herein is ancillary to the federal antitrust claim set out in Count One and arises from the same transaction and from a common nucleus of operative facts as alleged in Count One.

32. Plaintiff repeats and realleges paragraphs 2 through 25, inclusive, of Count One of this Complaint with the same force and effect as though each of said paragraphs had been set forth in full herein as part of this Count Three.

33. Plaintiff has had, during the period of time covered by this Complaint, actual contractual relationships with both consumers and practicing dentists, and a reasonable expectation of additional prospective business relationships with both consumers and practicing dentists, both existing and new. DELTA was aware of the existence of those contractual and prospective relationships.

34. DELTA intentionally disrupted and interfered with plaintiff's contacts and prospective business relationships. As a proximate result of DELTA's conduct, plaintiff has lost actual contracts and has been prevented from consummating prospective business transactions which would have yielded substantial profit to SMILECARE.

35. DELTA's intentional disruption of SMILECARE's actual contractual relationships and SMILECARE's prospective business relationships was carried out with malice and DELTA was guilty of fraud and oppression. By reason of such conduct, SMILECARE is entitled to both actual and exemplary damages.

COUNT FOUR

(Trade Libel)

36. Count Four of this Complaint is based on supplemental jurisdiction in that the claim asserted herein is ancillary to the federal antitrust claim set out in Count One above and arises from the same

transactions and from a common nucleus of operative facts as alleged in Count One.

37. Plaintiff repeats and realleges paragraphs 2 through 25, inclusive, of Count One of this Complaint with the same force and effect as though each of said paragraphs had been set forth in full herein as part of this Count Four.

38. Beginning at least as early as 1989, the exact date being unknown to plaintiff, and continuing up to the filing of this Complaint, DELTA, without justification, and without privilege published numerous disparaging statements about SMILECARE, its "Coverage Plus" program and the standard of care of its providers.

39. DELTA's statements about SMILECARE, its actuarial soundness, and its standard of care were false and misleading statements and disparaged SMILECARE's providers and SMILECARE's "Coverage Plus" product in that DELTA falsely stated that, in substance and effect, SMILECARE was a fraud.

40. DELTA's statements about SMILECARE and Coverage Plus were false.

41. As a direct and proximate result of DELTA's publication of these libelous statements, current and prospective consumers and providers have been deterred from dealing with SMILECARE.

42. DELTA's acts of trade libel and disparagement were done knowingly, willfully and maliciously and with intent to injure and oppress plaintiff and, by reason thereof, plaintiff is entitled to exemplary and punitive damages.

COUNT FIVE

(Unfair Competition Under Cal. Bus. & Prof. Code)

43. Count Five of this Complaint is based on supplemental jurisdiction in that the claim asserted herein is ancillary to the federal antitrust claim set out in Count One above and arises from the same

transactions and from a common nucleus of operative facts as alleged in Count One.

44. Count Five of this Complaint is filed pursuant to Sections 17200, et. seq. of the Business and Professions Code of the State of California.

45. Plaintiff repeats and realleges paragraphs 2 through 24, inclusive, of Count One of this Complaint with the same force and effect as though each of said paragraphs had been set forth in full herein as part of this Count Five.

46. DELTA has unilaterally and unfairly interpreted the co-payment requirement in its Participating Dentist Agreement to preclude patients from purchasing supplemental dental health plans.

47. DELTA's position regarding the co-payment requirement is illegal in that it directly contravenes California Health & Safety Code § 1371.2.

48. As a direct and proximate result of DELTA's unfair competition, consumers have been deprived of needed dental care and SMILECARE has been injured in its business and property.

COUNT SIX

(Breach of Contract)

49. Count Six of this Complaint is based on supplemental jurisdiction in that the claim asserted herein is ancillary to the federal antitrust claim set out in Count One above and arises from the same transactions and from a common nucleus of operative facts as alleged in Count One.

50. Plaintiff repeats and realleges paragraphs 2 through 25, inclusive, of Count One of the Complaint with the same force and effect as though each of said paragraphs had been set forth in full herein as part of this Count Six.

51. At DELTA's insistence, SMILECARE dentists submit

dental bills to DELTA through Dr. Hardin, SMILECARE's dental director and employee.

52. SMILECARE is contractually entitled to all reimbursements for services performed by its provider dentists.

53. Under DELTA's Participating Dentist Agreement, DELTA is obligated to pay a provider his or her accepted schedule of Usual, Customary and Reasonable fees.

54. DELTA breached this agreement by not paying to SMILECARE the accepted schedule of Usual, Customary and Reasonable fees submitted by SMILECARE dentists.

55. SMILECARE and its dentists have at all relevant times satisfied and performed their duties, obligation, terms and conditions under the Participating Dentist Agreement, except to the extent waived, excused or made impossible by the conduct of DELTA.

56. As a direct and proximate result of DELTA's breach of the Participating Dentist Agreements, SMILECARE has been damaged in an amount not yet ascertained but subject to proof at trial.

WHEREFORE, plaintiff prays that the Court adjudge and decree as follows:

1. That defendant has monopolized or attempted to monopolize the business of providing dental health care services in California in violation of Section 2 of the Sherman Act as alleged in Count One;

2. That judgment be entered for plaintiff against defendant for treble the amount of damages sustained by plaintiff as provided for by Section 4 of the Clayton Act (15 U.S.C. 15), a reasonable attorneys' fee, as provided by that statute, and costs of suit;

3. That defendant has violated Section 1371.2 of the Health and Safety Code of the State of California;

4. That judgment be entered for plaintiff based on that

statute for the amount of its actual damages;

5. That defendant has interfered with plaintiff's actual contractual relationships and with plaintiff's prospective business relationships, and that it did so intentionally, and with malice, fraud and oppression;

6. That plaintiff recover its actual as well as exemplary damages for defendant's tortious interference with plaintiff's actual contractual relationships and prospective business relationships;

7. That plaintiff recover its actual as well as exemplary damages for defendant's trade libel.

8. That defendant has competed unfairly in violation of Sections 17200 et. seq. of the Business and Professions Code of the State of California;

9. That defendant be adjudged to have breached its provider agreements with SMILECARE and its dentists and that plaintiff recover its actual damages for breach of contract.

10. That plaintiff be restored defendant's unjust enrichment and secure such equitable relief as it warranted;

11. That the Court permanently enjoin DELTA from engaging in further unlawful acts and practices;

12. That plaintiff have such other and further relief as the Court may deem just and proper.

DATED: February 24, 1994

BLECHER & COLLINS
MAXWELL M. BLECHER
ALICIA G. ROSENBERG
BENJAMIN D. NIEBERG

By s/Alicia G. Rosenberg
Alicia G. Rosenberg
Attorneys for Plaintiff
SMILECARE DENTAL GROUP

C-17

DEMAND FOR JURY TRIAL

Plaintiff hereby demands trial by jury pursuant to Rule 38(b), Federal Rules of Civil Procedure (28 U.S.C. Rule 38) and Local Rule 3.4.10.

Dated: February 24, 1994

BLECHER & COLLINS
MAXWELL M. BLECHER
ALICIA G. ROSENBERG
BENJAMIN D. NIEBERG

By s/Alicia G. Rosenberg
Attorneys for Plaintiff
SMILECARE DENTAL GROUP

PROOF OF SERVICE

The undersigned certifies that:

I am and was, at all times herein mentioned, a citizen of the United States and a resident of the County of Los Angeles, State of California, over the age of 18 years and not a party to or interested in the within action, and that my business address in 611 West Sixth Street, Suite 2000, Los Angeles, California. I further certify that I am employed int he office of a member of the Bar of this Court as whose direction the service was made. On February 25, 1994 I served the foregoing document entitled FIRST AMENDED COMPLAINT FOR DAMAGES AND EQUITABLE RELIEF by placing a copy in a sealed envelope with postage thereon and sending it by Federal Express to the below-listed party(ies) as follows:

M. Laurence Popofsky, Esq.
Robert A. Rosenfeld, Esq.
Matthew L. Larrabee, Esq.
HELLER, EHRMAN, WHITE & MCAULIFFE
333 Bush Street
San Francisco, CA 94104-2878

s/Celeste M. Gallegos
Celeste M. Gallego

## PROOF OF SERVICE BY MAIL

*State of California*

*ss.*

*County of Los Angeles*

I, the undersigned, say: I am and was at all times herein mentioned, a citizen of the United States and a resident of the County of Los Angeles, over the age of eighteen (18) years and not a party to the within action or proceeding; that my business address is 611 West Sixth Street, Suite 2000, Los Angeles, California 90017; that on October 3, 1996, I served the within *Petition For Writ of Certiorari* in said action or proceeding by depositing true copies thereof, enclosed in a sealed envelope with postage thereon fully prepaid, in the United States mail at Los Angeles, California, addressed as follows:

Clerk, United States Supreme Court
One First Street, N.E.
Washington, D.C. 20543
*(By Certified Mail: Original and Forty Copies)*

Laurence A. Weiss
Heller Ehrman White & McAuliffe
333 Bush Street
San Franscisco, CA 94104-2878

I declare under penalty of perjury that the foregoing is true and correct. Executed on October 3, 1992, at Los Angeles, California.

s/Celeste M. Gallegos
Celeste M. Gallegos